



A REPORT
TO THE
ARIZONA LEGISLATURE

Accounting Services Division

Compliance Review

Duncan Unified School District No. 2

Year Ended June 30, 2004



Debra K. Davenport
Auditor General

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DEBRA K. DAVENPORT, CPA
AUDITOR GENERAL

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

WILLIAM THOMSON
DEPUTY AUDITOR GENERAL

February 8, 2006

Governing Board
Duncan Unified School District No. 2
P.O. Box 710
Duncan, AZ 85534-0710

Members of the Board:

We have reviewed the District's audit reports and Uniform System of Financial Records (USFR) Compliance Questionnaire for the year ended June 30, 2004, prepared by Heinfeld, Meech & Co., P.C. to determine whether the District substantially complied with the USFR.

As a result of our review, we noted significant deficiencies in internal controls that indicate the District had not complied with the USFR. District management should implement the recommendations we have described in this report within 90 days after the date of this letter. We have communicated specific details for all deficiencies to management for correction.

During the 90-day period, the District may request a meeting to discuss these recommendations with my Office and the Arizona Department of Education by calling Magdalene Haggerty, Accounting Services Director, or Michael Stelpstra, Accounting Services Manager.

A member of my staff will call the Business Manager in several weeks to discuss the District's action to implement these recommendations. After the 90-day period, my staff will schedule an on-site review of the District's internal controls to determine whether the District is in substantial compliance with the USFR. Our review will cover the deficiencies we have communicated to management as well as any other internal control deficiencies we are aware of at the time of our review.

Sincerely,

Debra K. Davenport
Auditor General

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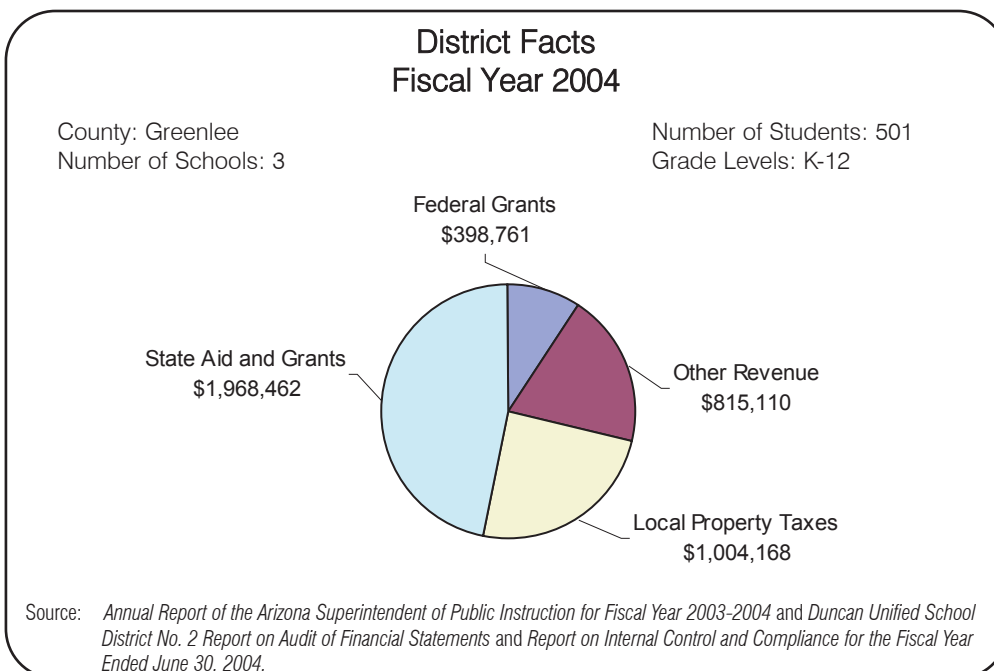
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INTRODUCTION

Duncan Unified School District No. 2 is accountable to its students, their parents, and the local community for the quality of education provided. The District is also financially accountable to taxpayers for over \$4.1 million it received in fiscal year 2004 to provide this education.

The District should use effective internal controls to demonstrate responsible stewardship for the tax dollars it receives. These controls are set forth in the *Uniform System of Financial Records* (USFR), a joint publication of the Office of the Auditor General and the Arizona Department of Education (ADE). The policies and procedures in the USFR incorporate finance-related state and federal laws and regulations and generally accepted accounting principles applicable to school districts. Districts are legally obligated to comply with USFR requirements, and doing so is good business practice.

As a result of our review of the District's audit reports and USFR Compliance Questionnaire for the year ended June 30, 2004, we determined that the District had failed to comply with the USFR. We noted certain deficiencies in controls that the District's management should correct to ensure that it fulfills its responsibility to establish and maintain adequate financial stewardship and to comply with the USFR. Our recommendations are described on the following pages.



The District should strengthen controls over competitive purchasing and expenditures

The District did not always follow competitive purchasing requirements or USFR guidelines and, therefore, may not have received the best value for the public monies it spent.

School District Procurement Rules for competitive sealed bidding and USFR guidelines for purchases below the bid threshold promote open and fair competition among vendors. This helps ensure that districts receive the best possible value for the public monies they spend. However, the District did not always follow the procurement rules or the USFR guidelines. For example, the Governing Board did not always determine in writing that only one vendor supplied the item or service for sole source procurements. Also, the District did not always obtain oral or written price quotations for purchases that required them. In addition, the District did not prepare purchase orders before goods and services were ordered and did not always record expenditures in the correct fiscal year.

Recommendations

To strengthen controls over competitive purchasing and expenditures and to comply with School District Procurement Rules and USFR guidelines, the District should perform the following:

- School District Procurement Rules provide the requirements for:
- Competitive sealed bids for goods and services in excess of \$33,689.
 - Competitive sealed proposals for goods and services when factors other than the lowest cost are appropriate.
 - Sole source and emergency procurements and other exceptions.

USFR guidelines require:

- Oral price quotations for purchases between \$5,000 and \$15,000.
- Written price quotations for purchases between \$15,000 and \$33,689.
- Determine whether to request oral or written price quotations or issue invitations for bids by analyzing the known requirements for an item or a collection of items that, in the aggregate, may result in purchases above the competitive purchasing thresholds.
- Issue invitations for bids or requests for proposals for purchases of construction, materials, or services exceeding \$33,689.
- Obtain written price quotations from at least three vendors for purchases estimated to cost between \$15,000 and \$33,689, and oral price quotations from at least three vendors for purchases estimated to cost between \$5,000 and \$15,000. If the District cannot obtain three price quotations, it should document the vendors contacted and their reasons for not providing quotations.
- Award a contract for a material, service, or construction item without competition only when the Governing Board determines in writing that there is only one vendor that supplies the item or service. Documentation of this determination should be retained in the purchasing file. Sole source procurements should be avoided, except when no reasonable alternative vendor exists.

- Prepare and approve purchase orders for all district expenditures, except exempted items, before ordering goods and services.
- Pay for goods or services received by June 30 during the year or the 60-day encumbrance period following June 30. Goods or services received after June 30 should be paid for in the next fiscal year.

USFR page VI-G-1 describes when purchase orders are required.

The District should ensure the accuracy of its student attendance records

The State of Arizona provides funding to school districts based on membership and absences. In turn, the State requires school districts to maintain accurate attendance records to ensure that the District receives the appropriate amount of state aid and local property taxes. However, the District did not maintain accurate attendance records since it did not always record partial-day absences accurately, and membership and absence days reported in the District's attendance records did not agree to ADE's reports. In addition, entry and withdrawal dates recorded in the computerized attendance system did not always agree to the entry and withdrawal forms or the teacher attendance registers. Further, students with ten consecutive unexcused absences were not always withdrawn correctly, and the District did not prorate membership for high school students enrolled in fewer than four subjects.

The District may not have received the appropriate amount of funding since the District did not record membership and absences correctly.

Recommendations

To help ensure that the District receives the correct amount of state and local funding, the District should record and report membership and absences, including partial-day absences, in accordance with ADE's *Instructions for Required Reports*. A second employee should verify that membership and absences reported to ADE are calculated accurately and agree with attendance records, including teacher attendance registers. Also, employees should accurately post the entry and withdrawal dates to teacher attendance registers and the computerized attendance system. In addition, the District should withdraw students absent for 10 consecutive unexcused days so that these students are only counted in membership through the last day of attendance.

ADE provides guidance for attendance reporting requirements in its *Instructions for Required Reports*.

The District should maintain accurate capital assets and stewardship lists

The District did not effectively account for its assets since the capital assets and stewardship lists were incomplete.

The District has invested a significant amount of money in its capital assets, which consist of land, buildings, and equipment. In order to safeguard its investment and help ensure accurate capital asset balances, effective stewardship requires the District to maintain accurate lists of these assets. However, the District did not accomplish this objective. Specifically, items located on the District's premises were not always included on the stewardship list, and equipment items were not tagged or identified by any other means. In addition, the District's capital assets list included some items more than once, and capital expenditures were not reconciled to items added to the lists. Finally, depreciation expense was not always recorded in the function for which the asset was used.

Recommendations

The following procedures can help the District improve control over its assets and ensure that its capital assets and stewardship lists are accurate and complete:

- Prepare and maintain a capital assets list that includes all equipment, land, buildings, and related improvements costing \$5,000, or the District's capitalization threshold if less than \$5,000, or more with useful lives of 1 year or more.
- Prepare and maintain a stewardship list that includes all equipment, including vehicles, costing between \$1,000 and the capital asset threshold.
- Affix a permanent tag with an identifying number to each equipment item costing \$1,000 or more, or specifically identify the assets on the lists by some other means such as serial numbers.
- Record capital asset items at actual costs, including ancillary charges such as sales tax, delivery, installation, and assembly.
- Reconcile items added to the lists during the fiscal year to capital expenditures annually, and the current year's capital assets list to the previous year's capital assets list. Make all necessary corrections.
- Record depreciation expense for each depreciable asset in the function for which the asset is used.

The form on USFR page VI-E-13 may be used to document the reconciliation of capital assets additions to capital expenditures.

The District's accounting records should be accurate and supported by documentation

The District's Governing Board depends on accurate information to fulfill its oversight responsibility. The District should also report accurate information to the public and agencies from which it receives funding. To achieve this objective, management should ensure that its accounting records and reports are accurate and complete and that transactions are properly recorded and authorized. However, the District did not fully accomplish this objective. Specifically, the District incorrectly recorded state grant revenue as local revenue in a federal fund, improperly classified expenditures and transfers, and did not ensure that interest revenue was properly allocated to its various capital projects funds. In addition, the District did not ensure journal entries were reviewed and approved prior to posting them in the accounting records, and did not always retain supporting documentation. Also, the District had an unreconciled difference between its records of cash balances and the County Treasurer's records.

The District did not always record transactions properly in its accounting records or ensure that journal entries were supported and approved.

Further, the District's year-end food service, supplies, and warehouse inventory lists were not complete as the lists did not include cost or calculate cost extensions. Additionally, the District did not retain documentation to support the approved daily route miles and handicapped extended school year miles reported to ADE, and reported the incorrect amount of miles on its budget worksheets. Finally, the District did not accurately report capital asset information in its annual financial report and omitted the Auxiliary Operations Fund from the report.

Recommendations

The following procedures can help the District record and report accurate accounting information:

- Classify all transactions in accordance with the USFR Chart of Accounts.
- Require a supervisor to review and approve journal entries before they are posted to the accounting records. Retain documentation for all journal entries, including evidence of authorization.
- Review the County's apportionment of interest earned on pooled investments and make any necessary adjustments.
- Reconcile records of cash balances to the County Treasurer's records at least monthly, investigate all differences, and make appropriate corrections.

USFR §III provides guidance for classifying financial transactions.

- Prepare inventory lists annually that include item and unit descriptions, purchase document numbers, quantities, unit costs, extended costs, page totals, and grand total.
- Prepare and retain documentation to support the number of routes, route miles traveled, eligible students transported, and handicapped extended school year miles reported on its Transportation Route Report.
- Calculate transportation funding in the budget worksheets based on amounts from the prior year's Transportation Route Report submitted to ADE.
- Require a second employee to verify that amounts reported on the AFR agree with the accounting records before it is submitted to the County School Superintendent and ADE.

The District should improve controls over cash and bank accounts

Poor cash controls left district monies susceptible to loss, theft, or misuse.

The District receives cash from various sources including extracurricular activities fees tax credits and auxiliary operations sales, and maintains bank accounts to deposit the related receipts. Because of the relatively high risk associated with cash transactions, the District should have effective internal controls to safeguard cash and ensure that it is promptly and accurately recorded and deposited in the bank accounts. These controls require that the District deposit cash receipts at least weekly, issue checks only for allowable purposes, and maintain an accurate record of transactions. However, the District did not deposit auxiliary operations and extracurricular activities fees tax credit receipts in a timely manner, and did not maintain check registers for two bank accounts. In addition, the District issued a check from the Maintenance and Operation Fund revolving bank account that was made payable to cash. Finally, the District had over \$46,000 of its bank balances that were uninsured and uncollateralized.

Recommendations

To improve controls over cash receipts, disbursements, and bank accounts, the District should:

- Deposit all cash receipts daily, if significant, or at least weekly in the appropriate bank account.

- Maintain a check register for each bank account to record all deposits and checks.
- Properly complete checks before issuing them to the payees. Make checks out to a specific payee and not to cash or bearer.
- Ensure that monies in bank accounts are secure by obtaining a collateral agreement with the bank for any amount on deposit in excess of federal depository insurance.